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Assessment of Certain Classes of Real Estate Under Depression Conditions

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EDITORIAL COMMENTS

ASSESSMENT OF CERTAIN CLASSES OF REAL ESTATE UNDER DEPRESSION CONDITIONS

THE depression has added greatly to the burden of the courts in reviewing assessments for taxation of real estate and other property. This is not only because stringent financial conditions tend to encourage and almost compel property owners to resist assessments which they regard as too high, but also because the very existence of the depression has greatly affected valuations, and has thereby made the problem of the proper distribution of the tax burden more difficult. It is the purpose here to discuss a few recent court decisions, where the property concerned was affected not only by depression conditions, but by peculiar circumstances of its own which would increase the difficulty of its proper valuation even in periods of reasonable prosperity.

Of such property, that of railroads is a typical example. To determine a reasonable market value for railroad property is difficult if not impossible, even in normal times. This difficulty is heightened by the depression, as is shown in the recent, but already famous, decision of the Circuit Court of Appeals for the Third Circuit in *Lehigh Valley R. Co. v. Martin,* 100 Fed. (2d) 139 (1938), involving New Jersey property taxes.

This case could actually have been decided as a matter of procedure. The railroads, having originally sued in the state courts, were held precluded from suing in the federal courts, under the doctrine of *res judicata.* However, the court did consider the merits of the case and indicated that relief would be refused apart from the procedural bar. The court did admit that the method of assessment used by New Jersey was seriously defective and should be revised by the legislature. But, of course, it is clear that a merely clumsy method of assessment does not call for judicial correction. More serious was the suspicion so strongly held that it was referred to by the court, "that the State of New Jersey seeks to maintain itself by taxing the appellants more and its other inhabitants less." Clearly if this was a fact the assessment was invalid. But the court, while apparently sharing to some extent the suspicion, refused relief because it was only a suspicion; such discrimination must be proved. The court several times cited *Great Northern R. Co. v. Weeks,* 297 U. S. 135, 56 Sup. Ct. 426 (1936), 1 LEGAL NOTES 32 (March, 1936), but declined to follow the apparent doctrine of that case that the court should give relief on a mere showing of substantial overvaluation without a showing of discrimination. Thus the court criticizes the method of valuation, and admits some grounds for suspicion of discrimination; but it refuses relief because that discrimination is not proved.

Another interesting problem is presented by the decision of the District Court of Minnesota in *Minnesota v. Federal Reserve Bank of Minneapolis,* 25 Fed. Supp. 14 (1938). Here the problem was as to the proper valuation of the building of the Federal Reserve Bank of Minneapolis. The building is concededly well located and well constructed; but its valuation would be difficult even in normal times, because of peculiar features of its construction. It is architecturally somewhat unusual, and it is designed not so much for ordinary commercial banking but primarily for the safeguarding of its assets; in other words, it is to a large extent a fortress rather than a commercial building.

To increase the difficulty, it appeared that for the years in question and for several years before, business property in Minneapolis, even of the most usual sort, was practically unsalable because of depressed business conditions. This obviously greatly increased the difficulty of determining any reasonable market value of the property.

The assessor worked out various scientific schemes of valuation, such as cost less physical depreciation with some further allowance for obsolescence, the results of which the court approved. The bank insisted upon a valuation based upon a calculation of purely theoretical income from the property, based on supposed use for ordinary commercial purposes. It is well settled that income from commercial property is an important, and sometimes the most important, factor in computing its value. (*Detroit v. Detroit and Canada Tunnel Co.,* 92 Fed. (2d) 833 (1937) 3 LEGAL NOTES 329 (March, 1938).) But here the property was not being used primarily for income producing purposes, and furthermore the income relied on by the taxpayer was purely theoretical. The court therefore seems right, especially as the taxpayer's calculations reduced this comparatively new and well constructed bank building to practically scrap value for tax purposes.

The chief criticism which could possibly be made is that the court may have sanctioned a valuation on some theory other than market value. The theory of assessment on any other basis than market value is generally and properly condemned. Perhaps the leading case is *State ex rel. Northwestern Mut. Life Ins. Co. v. Weiher,* 177 Wis. 445, 188 N. W. 598 (1922). On the other hand, the mere fact that property cannot presently be sold does not mean that it has no value for tax purposes; otherwise, all the business center of Minneapolis (and no doubt many other cities) would have been non-taxable during the worst of the depression. It seems that the assessor used the best method possible for computing a fair value for the building; in any case, it appears that he endeavored to put upon the bank its fair share, but only its fair share, of the property tax burden. In other words, no discrimination was intended; and none in substance resulted.

A third case on this general subject is the decision of the Court of Appeals of Ohio for Hamilton County in *Linch v. Heuck,* 16 N. E. (2d) 613 (1938). Here, unlike the cases previously discussed, ordinary residence property was involved; but the case presented what the court called "a rather unique situation." This was because the owner so desired this particular piece of land that he paid very much more than the normal price for it, and then bought it under a condition that he should erect an elaborate residence, much more costly than would be ordinarily justified in that location. The result was that he spent approximately $180,000 for the land and building, whereas, as the court admits, the selling price would probably not exceed $50,000. While it is not unusual for a person to find that he has spent more for his home than he can sell it for, such an extreme variation is certainly extraordinary.

The original assessent made by the county auditor was on a cubic content basis ordinarily used for residences, but with a reduction of 21 percent because of the extravagance in location and construction. This gave him a figure of $94,600, or about half the actual cost. The house was new, so there was no substantial physical depreciation.

The tax commission reduced the assessment to $76,340, the basis of the reduction not appearing. The owner appealed to the court, which made a further reduction to $50,000.

The Court of Appeals reversed the trial court and reinstated the $76,340 assessment of the tax commission. The court reached this conclusion on the simple ground that there was no showing that the tax commission had reached a wrong figure, holding that a court has no jurisdiction to reverse the assessing authorities merely because it disagrees with them.

These cases seem to indicate that the courts are not going to unreasonably interfere with the efforts of assessing officers to distribute the burden of property taxation in these troublesome times, so long as this effort is made with reasonable fairness and intelligence. The property owner cannot upset an assessment merely because it seems high even to the court, or because the method of assessment seems subject to some criticism. Nor can he upset an assessment merely because the property is temporarily unsalable or that a definite market value for his particular kind of property would perhaps always be more or less a matter of speculation. To obtain judicial relief he must show that there is a definite and rather serious discrimination, so that he is having imposed upon him an unfair share of the property tax burden of the locality. This is all as it should be, and it is to be hoped that other courts will follow the same rules. So far as *Great Northern R. Co. v. Weeks, supra,* seems to sanction judicial interference without a showing of discrimination, it should be overruled. But all this does not remove—indeed it emphasizes—the desirability and necessity of every possible effort to perfect the assessment process, so as to give the best results possible.

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